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C O N F I D E N T I A L KUWAIT 001535

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SUBJECT: CHEVRON AND KNPC SEEKING COMPROMISE ON NEUTRAL
ZONE REFINERY

REF: KUWAIT 1396

Classified By: CDA Alan G. Misenheimer for reasons 1.4 (b) and (d)

¶1. (C/NF) In an 8 October meeting with CDA, Kuwait National Petroleum Company (KNPC) Chairman and Managing Director Sami Al-Rushaid said discussions on the proposed location for a 615,000 bpd KNPC refinery in the Partitioned Neutral Zone next to the Saudi Arabian Chevron (SAC) compound were back at the company-to-company (KNPC to SAC) level after having been raised to the government-to-government (GOK to KSA) level (reftel). Al-Rushaid said he and his staff had personally met with the Saudi Arabian Chevron (SAC) management in the previous week to seek a compromise that would meet the needs and address the concerns of both companies. He said he was encouraged that SAC seemed "much more flexible" than in previous discussions. Jeff Ewing, Assistant to the President of SAC, told econoff separately that following the latest government-to-government discussions on this issue (most likely the 25 September visit of former Kuwaiti Oil Minister Abdulrahman Al-Atiqi to Jeddah to deliver a letter from Amir Shaykh Sabah to King Abdullah) the KSA had directed SAC to seek a compromise with KNPC that would include allowing KNPC to build the new refinery on land that was reserved for SAC.

¶2. (C/NF) In the KNPC-SAC discussions, compromise proposals were put forward by both companies. Ewing said that SAC offered an alternative site in its reserved area that would be slightly inland, further away from the SAC compound, and closer to the Al-Zour South power plant. Ewing acknowledged that moving the site inland would require KNPC to pipe water back and forth across the SAC compound. Al-Rushaid said KNPC had offered proposals to allay SAC's concern that the presence of the refinery on the waterfront would restrict SAC's ability to produce boiler feed water for its prospective large-scale steam flood program. KNPC offered to either produce the feed water itself and provide it directly to SAC or to allocate space within the refinery compound for SAC to produce its own feed water. Al-Rushaid suggested KNPC might also offer to purchase all of SACs crude product or at least offer to process SACs crude for export.

Comment

¶3. (C/NF) The apparent de-escalation of this issue from a political matter to a business negotiation is a positive development. Chevron seems less than delighted with the marching orders it has received from the KSA, but the latest developments offer hope that both companies might reach a solution that would allow construction of this critically important refinery to commence while preserving Chevron's ability to proceed with its steam flood program should it decide to do so if and when the KSA decides to renew its concession, which is set to expire in February 2009. SAC

would still clearly prefer not to have a mega-refinery built in its backyard, but it now appears increasingly likely that the refinery can be built in a way that will not directly impact Chevron's operations.

¶4. (U) KNPC announced on 29 September that it had pre-qualified U.S. firm Foster Wheeler to bid on two of the five contract packages for the USD 14 billion refinery. For one of the other contract packages, KNPC is reported to be in talks with U.S. firm Fluor, which already holds the project management contract for the refinery.

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